Understanding Director Duties & Managing Conflicts of Interest in Council-Owned Corporations.

Introduction

Welcome to the second of our articles on council-owned corporations. In this article, we explore the respective duties of directors and shareholders and take a deeper look at the roles they play in a council-owned corporation within the governance landscape.

Councillors and council officers are policy-makers in council, as shareholder, and in some cases as a director of the council-owned corporation as well. Wearing different hats creates unique risks and requires clear separation of functions to operate effectively.

1. Understanding the role and power of Directors

A council-owned corporation is a legally distinct entity, usually a company under the Corporations Act 2001 (Cth) (Corporations Act).

In some cases, the council appoints directors who are councillors or council offficers, or external professionals with relevant skills (finance, law, business, engineering). Appointments are usually approved by council resolution, with terms defined in the company's constitution.

Directors' duties and powers come from the Corporations Act 2001 (Cth), the company's constitution, and the common law.

The directors of a council-owned corporation (whether councillors, executives or independents) are typically responsible for:

- managing the company's affairs;
- making strategic and operational decisions such as entering contracts, acquiring assets or hiring key staff;
- approving budgets, expenditures and investments (unless otherwise dealt with in a funding deed or other contract);
- approving policies and internal controls; and
- monitoring performance and risks, ensuring the company meets its objectives.

The Directors must also ensure compliance with the Corporations Act, in particular the following duties:

- Duty to act in good faith in the best interests of the company.
- Duty to avoid conflicts of interest.
- Duty of care and diligence.

Importantly, in company board meetings directors must prioritise the interests of the council-owned corporation, not the council. Directors of a council-owned corporation are not council staff, but they are accountable to the council as the shareholder of the company.

2. Understanding the role and power of the Shareholder (the Council)

Shareholders provide oversight but do not manage daily operations, that is the board's responsibility. It is important to note that in its role as shareholder, councillors act collectively through council resolutions, not individually like under Directors' powers.

As sole or majority shareholder, the council's powers are set out in:

- the Corporations Act, which governs general shareholder rights;
- the company's constitution, which may specify approval thresholds, director appointment processes, and decision-making rules; and
- other contracts such as shareholder agreements, and policies may clarify roles and manage expectations.

The key powers of the company's shareholder typically include:

- appointing and removing directors to ensure the board has the right skills and independence;
- voting on changes to the company constitution;
- approving fundamental transactions, such as winding up, mergers or certain types of restructuring; and
- monitoring performance through reporting, audits, and financial statements.

3. Common Conflict of Interest

Council-owned corporations carry inherent risks if governance is weak or independence is lacking. These risks can include:

- Shadow director issues: councillors or council executives may make decisions or give directions as if they were board directors, even when they are not formally appointed, which can create legal or financial risks for the council.
- Blurred lines of authority: when councillors or council officers serve both as board directors and council decision-makers, it can be unclear whether a decision is being made in the capacity of a director or a councillor/shareholder, increasing the potential for mistakes or legal problems.
- Conflicts between council and corporation interests: decisions that benefit the council or community but are not in the best interests of the corporation can create tension between commercial and public objectives. Conflicts may also arise when community expectations, such as pricing or service levels, clash with the corporation's financial or operational obligations.

Access to confidential information: Board members may receive commercial information that cannot be shared publicly with the council or community, creating potential governance and transparency challenges.

Without clear separation between council and corporation roles, the purpose of corporatisation is undermined. Performance, accountability and commercial outcomes can suffer, while both legal and reputational risks increase significantly.

4. Managing Conflicts of Interest

Effectively managing conflicts of interest is critical to the success of a council-owned corporation. This means keeping council's role as owner separate from the board's role in running the company. Robust governance frameworks, such as constitutions, shareholder agreements and council policies should clearly set out responsibilities, boundaries and expectations.

Some practical measures include:

- Appointment of independent directors: appoint commercially experienced, independent board members to strengthen objectivity and reduce political influence. Ideally, serving council officers should not be directors.
- Clear role separation: councillors act collectively as shareholders, while directors act in the best interests of the company.
- Formal processes: have rules for declaring and recording conflicts of interest, and make sure people step aside from decisions when they have a conflict.
- Training and induction: ensure councillors and officers understand director duties, shareholder responsibilities and how to manage conflicts in practice.
- Regular governance reviews: carry out periodic reviews of the corporation's governance structures, policies and board practices to make sure they remain fit for purpose, legally compliant and aligned with the council's objectives.

A successful council-owned corporation must be structurally and operationally independent, guided by a strong governance framework that promotes transparency and accountability. By maintaining independence, applying the above-mentioned tools and proactively managing conflicts, councils can protect the public interest and ensure their council-owned corporations operate as trusted and effective commercial partners.

Conclusion

Effectively managing a council-owned corporation requires more than simply establishing the entity, it depends heavily on clear role separation, good governance and proactive management of conflicts of interest. Councils that clearly distinguish between shareholder and director responsibilities, appoint independent directors and implement strong governance frameworks are best positioned to achieve both commercial and community objectives.

By maintaining independence, monitoring performance and regularly reviewing governance structures, council-owned corporations can operate efficiently, transparently and sustainably, while protecting public ownership and accountability.

The Muscat Tanzer team has extensive experience advising councils on the establishment and governance of council-owned corporations. We assist with director and shareholder frameworks and risk management. For guidance on setting up a council-owned corporation or strengthening governance in an existing entity, please contact our team.

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